



International Organization of Securities Commissions
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5 December 2014

Technical Director
International Ethics Standards Board for Accountants
545 Fifth Avenue, 14th Floor
New York, NY 10017 U.S.A.

Our Ref: 2014/JE/C1/IESBA/166

Subject Line: IESBA's Exposure Draft: *Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client*

Dear Sir:

The International Organization of Securities Commissions' Committee on Issuer Accounting, Audit and Disclosure (Committee 1) appreciates the opportunity to comment on the International Ethics Standards Board for Accountant's (the IESBA or the Board) Exposure Draft: *Proposed Changes to Certain Provisions of the Code Addressing the Long Association of Personnel with an Audit or Assurance Client* (the Paper). As an international organization of securities regulators representing the public interest, IOSCO is committed to enhancing the integrity of international markets through the promotion of high quality accounting, auditing and professional standards, and other pronouncements and statements.

Members of Committee 1 seek to further IOSCO's mission through thoughtful consideration of accounting, disclosure and auditing concerns, and pursuit of improved global financial reporting. Unless otherwise noted, the comments we have provided herein reflect a general consensus among the members of Committee 1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

Overall Comments

We support the Board's efforts in seeking ways to strengthen the provisions that address familiarity threats created by the long association of engagement team members with an audit client. We commend the Board for undertaking such a project that has the potential to positively affect the independence, objectivity and professional skepticism exercised by auditors. These traits continue to



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be the foundation upon which an effective audit can be conducted. As such, we continue to support, at a minimum, partner rotation as a means to address the familiarity threat built up as a result of serving on the same audit engagement for an extended period of time.

We observe that the Paper made reference to recent regulatory changes to the partner rotation requirements in some of our member jurisdictions as another touch point to support no change to the current seven-year time-on period requirement within the Code. However, we would like to bring to the Board's attention that two of the three examples used (Australia and the United Kingdom) continue to require a five-year time-on period. This period can then be extended to two additional years but such an extension is very rarely used in practice. We provide this clarification for the Board's consideration to re-evaluate whether the conclusion reached in the Paper continues to be appropriate.

While we support the Board's efforts, we note that the general provisions in the extant Code stated that "Familiarity and self-interest threats *are created* by using the same senior personnel on an audit engagement over a long period of time." Whereas the proposed language states that "Familiarity and self-interest threats which *may impact* an individual's independence, objectivity and professional skepticism, *may be created* by using the same personnel on an audit engagement over a long period of time." (Emphasis added). We believe this change in language from indicating threats are created to "threats...may be created" sends the wrong message to auditors and at the same time diminishes the effectiveness of the Code.

In addition to these general points, below we have included areas of significant concern that we believe the Board should address as it seeks to conclude its work on this project. We have organized our letter in two sections: the first section addresses rotation of members of the audit engagement team; the second section addresses other matters for the Board's consideration.

Matters Related to the Rotation of Audit Engagement Team Members

Rotation of Non-Partner Engagement Team Members

We agree with the Board that "any member of the audit team, not just senior personnel, could be associated with the audit client long enough to create threats to independence, depending on the nature of the role they perform." We believe the broad concept of rotation provides an opportunity for the audit engagement to be conducted by individuals with fresh minds who are best suited to perform an objective audit.

While partners on an engagement have a heightened level of responsibility for the engagement as compared to non-partners, like the Board, we believe the familiarity threat should not be narrowly



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focused on partners. However, of particular note, we believe the familiarity threat of non-partner engagement team members who “grew up” on an engagement should also be emphasized within the requirements. Though the familiarity threat should be assessed for all such individuals, it is particularly important for those non-partners who grew up on the engagement and then became a partner on the same engagement. While accumulated knowledge about the audit client may benefit audit quality, these benefits must be weighed against the significant threat of familiarity with respect to individuals who grew up on the engagement and the need for individuals with fresh eyes to conduct the audit.

We recognize the Board’s general provisions to address long association of all engagement team members but we believe the requirements should be significantly strengthened to appropriately address the familiarity threat of non-partner engagement team members who have grown up on the engagement. We think the time on and time off periods should be scaled according to the individual’s role on the engagement, that is, the seniority of the role and possibly the nature and extent of work performed.

Length of Time-Off

Engagement Partner

We commend the Board for proposing to increase the time-off period for the engagement partner (EP) to five years as we believe it is better than two years and has the potential to strengthen the provisions addressing the familiarity risk by decreasing the potential for the EP from serving fourteen of sixteen years on the audit client given the current two-year time-off period requirement. Having said this, we note that the Paper states:

“In respect of an audit of a public interest entity, an individual shall not be a key audit partner for more than seven years. After such time:

- An individual who has acted as the engagement partner at any time during the seven year period shall not be a member of the engagement team or provide quality control for the audit engagement for five years...”

While we do not object to the concept we believe the Board should clarify the provision to better articulate when the time-off period commences for “an individual who has acted as the engagement partner at any time during the seven year period”. In particular, if the partner has served less than seven years, takes a temporary one-year break in service (example, for parental leave) and thereafter wishes to return to the audit engagement team, we believe the Board should make clear its intent of



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whether time-off is required when the individual first steps off the engagement (for parental leave); or after a cumulative period of seven years from when the individual first started as a key audit partner.

Engagement Quality Control Reviewer

We believe the engagement quality control reviewer (EQCR) should be subject to similar rotation requirements as the EP. This is because, in addition to concerns regarding independence in appearance, the EQCR is responsible for evaluating the significant judgments the engagement team made and the conclusions it reached in formulating the report. As a result of the significance of the EQCR's role on the audit engagement, we believe they should be subject to similar time-off requirements as the EP to promote continued objectivity.

Other Key Partners

We believe that the Board should also consider whether rotation requirements should apply to key partners involved in the audits of major operating subsidiaries of a PIE, including those circumstances where a partner subsequently becomes audit engagement partner for the PIE itself or vice versa.

Consulting During the Time-Off Period

While we believe it is important for the engagement team to have access to technical experts within the firm, where consultation with technical experts is necessary we believe the Board should first promote consultation with experts who are not serving a time-off period for the related audit engagement. For example, where consultation with such individuals is not prudent due to the lack of available subject matter expertise then an engagement team that is part of a large, multinational audit firm or network of firms should be required to consult with technical experts elsewhere within the audit firm or network. An engagement team that is part of a small audit firm which has outsourced its technical consultation function (while retaining responsibility for decisions and the audit opinion) presumably will not face this issue because it will in any event consult with a third party technical expert who is not formerly the engagement partner. For other engagement teams not falling into either of the above categories it should be possible to consult with another expert internally or externally to the firm.

Audit Partners Switching Audit Firms

We note that the Paper is silent with respect to the familiarity threat when an audit partner switches firms and the new audit firm is also now responsible for auditing the audit client. We believe the rotation requirement is intended to address the need to have a fresh look with respect to the audit client. If the audit partner has a continuing relationship with the audit client as a result of employment



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with another audit firm that in turn now audits the audit client then we believe the audit partner's prior service while with the previous audit firm should count in the determination of the partner rotation requirement.

Transition to a PIE

We note the Paper states that:

“If the individual has served the audit client as a key audit partner for six or more years when the client becomes a public interest entity, the partner may continue to serve in that capacity with the concurrence of those charged with governance for a maximum of two additional years before rotating off the engagement.”

While we recognize the Board's efforts to strengthen the extant provisions by now requiring concurrence of those charged with governance when adding two additional years for a key audit partner who has served an audit client for six or more years when the client becomes a PIE, we do not believe the provisions go far enough. We believe the familiarity threat is consistent whether a partner is serving an audit client that is a non-PIE or a PIE. As such, we believe the total length of time a partner is allowed to serve a non-PIE audit client that becomes a PIE should be the same as required for a partner who has solely served as an audit partner on a PIE.

Other Related Matters

Outreach to Those Charged With Governance

As a result of the critical role of those charged with governance regarding matters thought to bear on the auditor's independence we believe that specific and concentrated outreach to this stakeholder group should be conducted during the feedback phase and other relevant stages of the project to gather their views on the Board's proposals.

Interplay between Partner and Firm Rotation

We recognize that the scope of the project does not cover audit firm rotation. However, since audit firm rotation is another approach being used by some jurisdictions to mitigate similar concerns being addressed by partner rotation, the Board should consider the interplay between the two approaches and determine how the Code would operate or be applied in those jurisdictions. For example, in the Netherlands it is foreseen that a firm may perform an audit for ten years. A long association provision for an EP of 7 years does not interplay well with this foreseen term for mandatory firm rotation; for example, a provision for five year EP terms would interplay better.



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Addressing Professional Skepticism in the Code

We would also like to use this opportunity to encourage the Board to determine how the concept of professional skepticism can be addressed more thoroughly in the Code, not just with respect to partner rotation. We note the Code has a dedicated section addressing matters relating to auditor independence as this underlies everything the auditor does in performing the audit. In the same way, we believe professional skepticism underlies everything the auditor does in performing the audit and therefore may warrant a dedicated section and a similar level of emphasis within the Code. In this regard, we observe that the IESBA Strategy and Work Plan 2014-2018 includes a project on audit quality in which the Board "will consider the need for appropriate action to complement any further actions the IAASB may determine to pursue to contribute to improving audit quality." We believe a project undertaken by the IESBA to develop a dedicated section in the Code addressing professional skepticism could fulfill this goal and contribute to improving audit quality.

Thank you for the opportunity to comment on the Paper. If you have any questions or would like to further discuss these matters, please contact either Nigel James or me at 202-551-5300.

Sincerely,

Julie A. Erhardt
Chair
Committee on Issuer Accounting, Audit and Disclosure
International Organization of Securities Commissions